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of Accounting and Reporting
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Agenda item 5

ADOPTION OF THE REPORT OF THE GROUP ON ITS NINTH SESSION

Draft report

Addendum

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PROGRAMME OF WORK OF THE INTERGOVERNMENTAL WORKING GROUP OF EXPERTS ON INTERNATIONAL STANDARDS OF ACCOUNTING AND REPORTING

B. Discussion of accounting and reporting issues identified during the eighth session

2. Accounting for environmental protection measures

1. At its 5th and 6th meetings, on 7 March 1991, the Group discussed accounting for environmental protection measures, as contained in the report of the Secretary-General (E/C.10/AC.3/1991/5). In introducing the item, the representative of the United Nations Centre for Transnational Corporations mentioned how the Group's previous report had sparked interest among other groups and institutes. There also appeared to be a growing awareness among securities regulators and business executives. The observer for the Fédération international des experts-comptables francophones (FIDEF) stated that developing countries were interested in enjoying a certain quality of life rather than being depots for the developed world's industrial wastes. Unfortunately, such quality was hard to

achieve because they did not have sufficient resources to set up control mechanisms or to monitor pollution. Therefore, developing countries were more dependent on international standards for protection. In the area of accounting, financial statements needed to begin to reflect the environmental risks and latent liabilities present in some business operations. More environmental information in financial statements would allow investors to choose less polluting investments. Where environmental information could not be quantified, it should at least be disclosed in the notes.

2. The observer for the International Confederation of Free Trade Unions (ICFTU) found the report to be excellent and the information disclosure required to be basic. Moreover, the Group had agreed at its eighth session on information disclosure necessary in the board of directors' report. She asked whether, in terms of environmental contingent liabilities, existing international standards covered their recognition and measurement. In responding to her question, the Secretary-General of IASC said he found the report useful and valuable. Regarding the rules for recognizing contingent liabilities, they were contained in IAS 1, 5, 10 and 11. However, the International Accounting Standards did not deal with information disclosure in the board of director's report since IASC restricted itself to financial statements themselves. He endorsed the view that at the present time it might be better to let things evolve and encourage best practices rather than laying down rules.

3. The expert from Brazil informed the Group that his country would act as host for the United Nations Conference on Environment and Development in 1992. If the Group wanted to encourage best practice among the preparers of financial statements, it could prepare a new report especially for that meeting in order to make colleagues aware of the issues. It would be a unique opportunity for the profession to be heard. He was of the opinion that, while formulating rigid rules should be avoided, some formulation of recommendations was necessary. Another expert said that some developing countries needed guidance now. For example, in his region there were serious environmental problems and they would have to be considered in the financial statements of both transnational corporations and domestic enterprises. The problem of environmental contingencies would be acute, whereas previously they had not existed to the extreme extent as had resulted from the Gulf war.

4. One expert reminded the Group that it had agreed at its eighth session that environmental protection measures were an important matter. The new review of industry practices had revealed that it was possible to segment environmental expenditures, current and capital. He noted that some enterprises had also experimented with resource-based accounting, which allowed them to monitor the impact of their operations on the environment. Enterprises also produced from time to time special purpose reports on the environment, since there were other interested parties in addition to financial users. However, despite new research and review, he wanted to refrain from issuing rigid rules. He suggested that the Group should continue to review the content of the board of directors' reports.

5. Another expert questioned whether the segmentation of environmental expenses was really as feasible as suggested in the report. He noted the presence of such words throughout the text as "estimates", "judgement" etc. The resultant amounts

were of a soft character, and so it was better at this point to leave it open to enterprises to do what was appropriate. Another expert responded that accountants always had a problem with estimates and the Group should not dwell on it. The important thing was to introduce the concept of "environmental accountability" and have environmental costs appear in board of directors' reports, financial statements and the auditors' reports.

6. The observer from FIDEF noted that the Group was an intergovernmental one and that while self-regulation was desirable, the Group should give some guidance in this area. Recommendations were needed both for the board of directors' report and the notes to financial statements. While IAS 1, 5, and 10 might be sufficient for normal contingent liabilities, he was not sure they were specific enough to deal with environmental liabilities. A number of experts from developing countries spoke of ensuring that companies provided a certain minimum information and that the recommendations should go beyond those of the eighth session. It might be advisable to split the recommendations into those that were accepted and those requiring further consideration.

7. Another expert stated that it was necessary to give a true and fair view of operations in financial statements and that they should correctly evaluate environmental measures. The report demonstrated that this evaluation was practicable. He favoured issuing conclusions regarding information disclosure in the report of the board of directors, as outlined in the report. However, he was hesitant on the question of contingent liabilities and thought it would be better to return to it at the ninth session after more review. A country observer related how the Group's previous report had stimulated a great deal of interest in his country and that it was not perceived as final. He said the Group needed to express its view on the current report in order to encourage others to start or continue work in that area.

8. The Group decided to leave the recommendations section of the report (part IV) in its entirety but to change its title to "Conclusions for consideration of Governments and interested parties". The text of paragraphs 64, 66 and 67 was amended, changing the "shoulds" to "coulds" so that the conclusions took on the quality of items to be considered rather than requirements.

9. Thus, the conclusions of the Group regarding the issue of accounting for environmental protection measures read as follows:

Conclusions for consideration of Governments and interested parties

10. The following are items that could be considered by the board of directors to be included in their report/management discussion in order to deal with relevant environmental issues:

(a) The type of environmental issues that are pertinent to the enterprise and its industry;

(b) The formal policy and programmes that have been adopted by the enterprise with respect to environmental protection measures (if no formal policy and programmes exist, it should be stated);

(c) The improvements in key areas that have been made since the introduction of the policy, or over the past five years, whichever is shorter;

(d) The environmental emission targets that the enterprise has set for itself, and how the enterprise is performing relative to those targets;

(e) The extent to which environmental protection measures have been undertaken due to governmental legislation and, if so, the extent to which governmental requirements (for example, a timetable for the reduction of emissions) are being achieved;

(f) Any material proceedings under environmental laws; management should disclose a known potentially significant environmental problem unless it can objectively conclude that the problem is not likely to occur or, if it does, that the effect is not likely to be material;

(g) The financial or operational effect of environmental protection measures on the capital expenditures and earnings of the enterprise for the current period and any specific impact on future periods;

(h) When material, the acutal amount charged to operations in the current period, together with a description of the environmental measures to which they relate. This amount might be subdivided into the following general ledger accounts:

(i) Liquid effluent treatment;

(ii) Waste gas and air treatment;

(iii) Solid waste treatment;

(iv) Analysis, control and compliance;

(v) Remediation;

(vi) Recycling;

(vii) Other (for example, accidents, safety etc.);

(Where it is not possible to segregate the amount that relates to environmental protection measures, this fact should be stated.);

(i) When material, the actual amount capitalized during the current period, the accumulated amount capitalized to date, and the period for amortizing, or writing off, such amounts, together with a description of the environmental measures to which they relate. This amount might be subdivided into the categories listed in (h). (Where it is not possible to segregate the amount that relates to environmental measures, this fact should be stated.)

11. As accounting policies are normally described in the notes to the financial statements, the following environment-related accounting policy notes could be included therein:

(a) Recording liabilities and provisions;

(b) Setting up catastrophe reserves (through appropriations of retained earnings);

(c) Disclosure of contingent liabilities.

12. As contingent liabilities are normally disclosed, if material, in the notes to financial statements, the following environment-related items could be included therein:

(a) Liabilities, provisions and reserves that have been set for the current period, and amounts accumulated to date;

(b) Contingent liabilities, with an estimate of the amount involved, unless the event is not likely to occur. The possible loss should be quantified to the extent reasonably practicable. If the possible loss cannot be reasonably calculated, a description of the contingent liability should continue to be furnished and the reason should be given why an estimate of the amount of the loss cannot be made. Completion of a feasibility study of remediation costs may be normally considered as the earliest date at which a reasonable estimate of the liability is possible.